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IN THE

Supreme Court of the United States

AT THE OCTOBER TERM, 1941.

315 U.S. 806

No. 823

SAMUEL INSULL, JR., ET AL.,
Cross-Petitioners (Defendants),

vs.

THOMAS D. AIKEN, ET AL.,
Cross-Respondents (Plaintiffs),

BRIEF OF CROSS-RESPONDENTS (PLAINTIFFS) IN OPPOSITION TO THE CROSS-PETITION FOR WRIT OF CERTIORARI.

EDMUND D. ADCOCK,
33 North La Salle Street,
Chicago, Illinois,

ROGER Q. WHITE,
120 South La Salle Street,
Chicago, Illinois,

LEWIS F. JACOBSON,
33 North La Salle Street,
Chicago, Illinois,
Counsel for Cross-Respondents (Plaintiffs).

THE GUNTHORP-WARREN PRINTING COMPANY, 310 WEST JACKSON, CHICAGO

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BRIEF OF CROSS-RESPONDENTS (PLAINTIFFS) IN OPPOSITION TO THE CROSS-PETITION FOR WRIT OF CERTIORARI.

MAY IT PLEASE THE COURT:

The Supreme Court should not entertain the defendants' cross-petition for writ of certiorari for the reason that the judgment which the cross-petitioners attack is not final.

The "cross-petition" by the defendants prays that the judgment of the Circuit Court of Appeals "may be reviewed in so far as the Circuit Court of Appeals reversed

the decree of the District Court for the Northern District of Illinois'' (defendants' cross-petition, p. 1). The District Court sustained certain motions of the defendants to dismiss the complaint as to the cause of action for improper payment of dividends for failure to state a cause of action (R. 269-297, 321) and denied the plaintiffs' motion for leave to file amendments to the complaint (R. 321). The Circuit Court of Appeals reversed that portion of the District Court's judgment and held that the original complaint stated a cause of action and that the plaintiffs should have been given leave to file their proffered amendments to the complaint (R. 358-363).

Other defenses asserted by defendants were unsuccessful. In the District Court defendants had also contended, as other grounds for dismissal, that the jurisdictional amount was not adequately alleged and that non-resident plaintiffs had been selected collusively to establish Federal jurisdiction. The District Court held against these contentions and found that it had jurisdiction of the parties and of the subject matter (R. 297). Upon defendants' motion to require plaintiffs' attorneys to show their authority to maintain this suit, the District Court heard evidence and decreed that such authority was established (R. 321). The District Court's decree also denied defendants' second motion for summary judgment by which they sought to bar this suit on the ground that covenants not to sue had been given by plaintiffs to four of the defendants (R. 321). Defendants took no appeal from any of these rulings, but on plaintiffs' appeal from the final decree defendants urged all of the defenses in which they had been unsuccessful as additional argument to sustain the decree of dismissal. In the Circuit Court of Appeals plaintiffs raised objection to the right of defendants to urge arguments as to authority to sue and covenants not to sue without having taken any cross-appeal. The effect of their failure to appeal is discussed in Point IV of this brief. However, the

Circuit Court of Appeals considered these arguments of the defendants and found them to be unsound (R. 352-363). The judgment order of the Circuit Court of Appeals, which the cross-petition seeks to review, is:

> "* * * the judgment of the said District Court in this cause appealed from be, and the same is hereby affirmed as to the cause of action relating to the pledges, and reversed as to the cause of action relating to the dividends; and that this cause be, and it is hereby, remanded to the said District Court with directions to proceed in accordance with the opinion of this Court filed in this cause." (R. 364.)

Obviously, the order of the Circuit Court of Appeals, in reversing that portion of the District Court's judgment relating to the improper payment of dividends, is not a final decree but is simply an intermediate or interlocutory order. It is an order which settles the sufficiency of the original complaint and grants leave to the plaintiffs to file amendments to the complaint. When this case goes back to the District Court, the amendments to the complaint will be filed and the only burden placed on the defendants will be to plead to the amended complaint. When the pleadings are closed and the trial takes place, the final decree may be entered on the merits in behalf of the plaintiffs. If that should happen, the defendants would still have the right, should the Circuit Court of Appeals affirm the District Court, to petition this Court for review by certiorari of the same questions, relating to the sufficiency of the complaint, the amendments and jurisdiction of the court, which they now seek to have this Court review prematurely. If, on the other hand, the final decree after trial should be in favor of the defendants, all the matters now raised by defendants' cross-petition for writ of certiorari would become moot.

The principle has been enunciated in many cases that the Supreme Court should not grant certiorari except

from final decrees. In *Hamilton-Brown Shoe Co.* v. *Wolf Bros. Co.*, 240 U. S. 251, this Court stated the rule as follows (p. 258):

> "As has been many times declared, this is a jurisdiction to be exercised sparingly, and only in cases of peculiar gravity and general importance, or in order to secure uniformity of decision." (citing cases)
>
> * * * * *
>
> "And, except in extraordinary cases, the writ is not issued until final decree." (citing cases)
>
> * * * * *
>
> "The decree that was sought to be reviewed by certiorari at complainant's instance was not a final one, a fact that of itself alone furnished sufficient ground for the denial of the application; * * *"

Of course, it may be true that this Court is not expressly prohibited by any statutory restrictions from considering petitions for certiorari addressed to interlocutory orders but the extent to which it should limit its jurisdiction is set forth in *American Construction Co.* v. *Jacksonville, T. & K. W. R. Co.*, 148 U. S. 372, in which Justice Gray said (p. 384):

> "Clearly, therefore, this court should not issue a writ of certiorari to review a decree of the circuit court of appeals or appeal from an interlocutory order, unless it is necessary to prevent extraordinary inconvenience and embarrassment in the conduct of the cause."

There is no showing made in the defendants' cross-petition for certiorari, nor could such a showing be made, that their petition should be granted in order to prevent "extraordinary inconvenience and embarrassment in the conduct of the cause." On the contrary, the defendants' cross-petition indicates no more than that the defendants desire to have this Court pass upon preliminary questions of pleadings.

This Court should not be burdened, by virtue of the

piecemeal review of a case, with the consideration of issues which may become moot by the time when the final decree shall be entered. For that reason alone the defendants' cross-petition should be denied, in which event the points raised in their cross-petition, together with our refutation of those points presented in the balance of this answer, become unimportant. However, we shall now answer the points argued in the cross-petition in the same order in which they are discussed in the cross-petition.

I.

The Circuit Court of Appeals correctly held that a cause of action was stated under the Illinois statute for declaring or assenting to dividends in impairment of capital or while insolvent and that the plaintiffs should have been given leave to file the proffered amendments to the complaint.

The defendants' cross-petition for certiorari involves only the cause of action under Section 23 of the Illinois Corporation Act of 1919, which provides:

> "The directors shall jointly and severally be liable for the debts and contracts of the corporation in the following cases: * * *
>
> (2) For declaring or assenting to a dividend if the corporation is, or is thereby, rendered insolvent, or its capital is thereby impaired, to the extent of such dividend; * * *"

The District Court sustained defendants' motions to dismiss as to this cause of action on the ground that the original complaint was lacking in details as to the dividends involved and was not sufficiently specific to charge any individual director with being present at any meeting when dividends were declared or assented to (R. 296-297). Thereupon, plaintiffs promptly submitted amendments (R. 299, 317) which set forth details as to each dividend and

the participation of each defendant therein, but the District Court denied leave to amend (R. 312-315, 319).

The Circuit Court of Appeals agreed with the District Court that the original complaint tends to be deficient in details, but was satisfied that it is not fatally deficient in any essential (R. 357-360). It further held that the District Court erred in refusing leave to the plaintiffs to file the amendments on the ground of delay in presenting them inasmuch as the record conclusively shows that the delay in disposing of the motions to dismiss was agreed to and acquiesced in by both sides and that the intervening period was devoted in the main to the settlement of the bank cases referred to in *Aiken* v. *Insull*, case No. 821 before this Court (R. 360). The Circuit Court of Appeals further held that the Statute of Limitations was no bar to the filing of the amendments because they merely stated the subject matter of the original complaint more fully and not as a new cause of action (R. 360).

Defendants made other contentions which the Circuit Court of Appeals considered and in respect to which it held against the defendants (R. 360-362). These contentions of the defendants, as well as their argument that the deficiency of details in original complaint was fatally defective and that the amendments should not have been permitted, are reiterated in Point I of cross-petitioners' brief and will be discussed by us in the following subdivisions of this Point I.

A. *The original complaint was sufficiently specific to charge all defendants for all dividends.*

In approaching this point, it must be borne in mind that amendments were tendered which amplified in detail the allegations which the District Court considered insufficient. Defendants' contention that the original complaint was not

sufficiently specific is relevant only to the question whether the original complaint was so deficient in failing to state any cause of action as to be fatally defective so that there was nothing to which the amendments could attach, thus giving rise to the question whether the amendments stated a new cause of action barred by the Statute of Limitations. If, on the other hand, the original complaint did state a cause of action, even though defectively, then, under the Rules of Civil Procedure, however deficient it may have been in details, it would be clearly erroneous to dismiss the suit for want of equity when plaintiffs have offered amendments as to that same cause of action which cure the defects and supply the details.

The allegations of the original complaint pertinent here are, in substance, as follows:

(a) About January 1, 1930, the plaintiffs and approximately 20,000 members of the public purchased, at approximately par, the $60,000,000 of 10-year 6% Series B debentures, issued by I. U. I. at that time, of which approximately $55,000,000 remained unpaid and outstanding in the hands of plaintiffs and the other members of the public at the time of filing suit (R. 11-12); and the holdings of each plaintiff are specified (R. 19). At the time of filing suit there were also outstanding in the hands of the public $2,469,000 of 20-year 5% Series A debentures issued by I. U. I. about January 1, 1929 (R. 6);

(b) All defendants in this suit constituted and served as the directors of I. U. I. continuously from January 14, 1929 until its bankruptcy, April 16, 1932 (R. 5);

(c) Certain of the defendant-directors, including the cross-petitioners, Insull, Jr., Doyle and Stuart, constituted and served as the Executive Committee and Finance Committee during the entire period (R. 5);

(d) During the entire existence of I. U. I. Section 23 of the Illinois Corporation Act of 1919, above referred to, was in effect (R. 33);

(e) On December 13, 1931, the total liabilities of I. U. I. exceeded the total fair market value of assets and ever since

that date I. U. I. has been wholly and irretrievably insolvent (R. 34);

(f) The outstanding capital stock of I. U. I. consisted of 40,000 shares Prior Preferred, 40,000 shares 1st Series Preferred, 450,000 shares 2nd Series Preferred and over 2,000,000 shares Common, all without par value (R. 17);

(g) On January 9, 1932, at a meeting attended by certain directors specifically named, the action of the Executive and Finance Committee in directing the payment, as of January 2, 1932, of a dividend of $1.39 per share on the Prior Preferred Stock, was unanimously ratified, confirmed and approved (R. 34);

(h) I. U. I. had no surplus at any time during the years 1929, 1930, 1931 and 1932 but nevertheless cash dividends were paid during each of said years on all classes of its preferred stock, the exact amounts of which cash dividends are unknown to the plaintiffs (R. 24, 34);

(i) The Board of Directors authorized or ratified the actions of the Finance or Executive Committee authorizing the payment of said dividends (R. 34);

(j) Each of said directors had or should have had, in the reasonable exercise of his duties, knowledge of all of said matters (R. 36);

(k) The relief prayed is for an accounting and judgment against defendants in favor of the plaintiffs and others similarly situated by virtue of the acts of defendants hereinabove complained of (R. 37).

For the purpose of the present discussion we do not deem it necessary to consider other allegations setting forth further particulars and evidentiary matter, such as the details of one of the dividends approved at the meeting of January 9, 1932 (Par. 43, R. 34) nor the allegations concerning fictitious income (Pars. 23-29; R. 22-24). As pointed out by the Circuit Court of Appeals (R. 359):

> "From a reading of the original complaint in its entirety, it is our conclusion that it sufficiently describes a cause of action against the defendants for the violation of Sec. 23 of the Corporation Act of 1919.

> We agree with the District Court that it tends to be deficient in details, but we are satisfied that it is not fatally deficient in any essential."

Defendants urge the argument that no present defendant is definitely connected with any act in declaring or assenting to any dividend. However, they do not cite any cases but rely only on their argument that the allegations are not specific and that no individual is charged and consequently the dividends may have been declared or assented to by persons other than cross-petitioners.

The original complaint alleges that all of the defendants were all of the directors during the entire period and charges *all* of them with authorizing or ratifying the declaration of all the dividends. How can it be said, therefore, that no individual director is charged with having done so? See *Loft, Inc.* v. *Corn Products Ref. Co.*, 103 F. (2d) 1, 9 (C. C. A. 7) (Cert. den. 308 U. S. 558).

Where there were a number of directors and a series of meetings at which allegedly wrongful acts took place, the failure to allege details as to attendance and voting does not justify a dismissal of the complaint as that is a matter of evidence (*Cosmopolitan Trust Co.* v. *Mitchell*, 242 Mass. 95, 136 N. E. 403).

The new Rules of Civil Procedure apply in this case. However, it is immaterial whether the original complaint in this case is tested by the former equity rules or by the new Rules of Civil Procedure because the allegations are sufficient whether tested under the former rules or the present rules.

Under Old Equity Rule 25 it was sufficient that a bill in equity should contain "a short and simple statement of the ultimate facts upon which the plaintiff asks relief, omitting any mere statement of evidence." Rule 18 of the former rules in equity provides that "* * * the technical forms of pleadings in equity are abolished."

Under the new Rules of Civil Procedure it is provided in Rule 8a (2) that a complaint shall contain

> "a short and plain statement of the claim showing that the pleader is entitled to relief,"

and in Rule 8e (1) that:

> "Each averment of a pleading shall be simple, concise, and direct. No technical forms of pleading or motions are required."

In *Securities and Exchange Commission* v. *Timetrust*, 28 Fed. Supp. 34 (D. C. N. D. Calif.), the court states (p. 41):

> "The modern philosophy concerning pleadings is that they do little more than indicate generally the type of litigation that is involved. A generalized summary of the case that affords fair notice is all that is required. Pleadings shall be so construed as to do substantial justice."

The same was held in the following cases:

Van Dyke v. *Broadhurst*, 28 Fed. Supp. 737 (D. C. Pa.);

Fidelity & Deposit Co. v. *National Banking Assn.*, 267 Fed. 367 (C. C. A. 4);

Leimer v. *State Mutual Life Assurance Co.*, 108 F. (2d) 302 (C. C. A. 8).

If a complaint is not sufficiently specific, defendants' remedy is a motion for a more specific statement (see Rule 12-e)—not a motion to dismiss. *Koser* v. *American Fruit Growers, Inc.*, 60 F. (2nd) 313, 315 (D. C. Pa.).

Under either the old Equity Rules or the new Rules of Civil Procedure it seems clear that where the facts upon which the complaint is based are peculiarly within the knowledge of the defendants, the rules must be interpreted even more liberally.

In *State* v. *Illinois Central R. R. Co.*, 246 Ill. 188, 92 N. E. 814, the court said (p. 237):

> "If a matter essential to the determination of the claims of complainant is charged to rest in the knowl-

> edge of the defendant or must of necessity be within his knowledge * * * precise allegations thereof are not required * * *, all the facts need not be set out in the bill. It is sufficient if general statements of fact are made, under which pertinent details can be proved."

Since it appears that there are no cases whatever with which defendants claim the decision of the Court of Appeals on this point is in conflict, and we have cited numerous authorities above to show that the decision is in accordance with the law and with good reason, defendants' application for certiorari on this ground should be rejected.

B. *The allegation that dividends were declared in the first instance by the Executive Committee and thereafter ratified by the Board of Directors, does not relieve the defendants from liability therefor.*

The Circuit Court of Appeals held that the Executive Committee was the creature and agent of all defendants, thereby rendering them liable for the dividends declared by the committee, irrespective of the subsequent ratification by the directors. The Circuit Court of Appeals also held that in any event those directors who were on the Executive Committee were liable for the dividends which they declared. Defendants claim these holdings are in conflict with the law of Illinois, citing *Lewis* v. *Montgomery*, 145 Ill. 30, but it is very apparent that there is no conflict since the facts are entirely distinguishable.

In the case at bar the Executive Committee consisted of some of the directors of I. U. I. All of the directors are defendants in this suit. Those on the Executive Committee were appointed to that Committee by all of the directors. By the by-laws which they adopted the directors empowered the Executive Committee to declare dividends between meetings of the Board (R. 221-222).

Lewis v. *Montgomery*, 145 Ill. 30, upon which defendants

place great reliance, did not involve the statutory liability for declaring dividends but involved the statutory liability for assenting to the creation of excessive indebtedness. The excessive indebtedness in that case was created by an employee of the corporation, whose position as superintendent entitled him to incur indebtedness. The court held that the directors could not rescind the valid obligation of the corporation and that it was their duty to recognize it and provide for its payment. Inasmuch as the directors took no part in creating the debt, the court properly held that their subsequent recognition of it as a valid obligation of the corporation did not constitute "assent" to the creation of indebtedness in excess of the statutory limitation within the meaning of that statute. This is distinguishable from the instant case because the power to declare dividends is solely in directors.

Ryder v. *Alton & S. Ry. Co.*, 13 Ill. 516.
Hamblock v. *Clipper Lawn Mower Co.*, 148 Ill. App. 618.
Robertson v. *Bucklen*, 107 Ill. App. 369.
Spellman on Corporate Directors, Sec. 141.

Certainly directors do not have a duty to pay improperly declared dividends. Even after a dividend has been declared but before it is paid, it could be revoked by the directors and could be enjoined if it would impair capital or render the corporation insolvent (*Coquard* v. *National Linseed Oil Co.*, 171 Ill. 480, 486). A stockholder could not compel payment of such an improperly declared dividend (*Hamblock* v. *Clipper Lawn Mower Co.*, 148 Ill. App. 618). Even after it has been paid, an improper dividend can be recovered from the stockholders who received it (*Johnson* v. *Canfield-Swigart Co.*, 292 Ill. 101, 116 and *Clapp* v. *Peterson*, 104 Ill. 26).

As pointed out above the Executive Committee did not consist of "employees" of the corporation, as was the

situation in *Lewis* v. *Montgomery,* but consisted of directors who were selected by all of the directors.

While directors of a corporation may delegate their duties to others they may not delegate their responsibility:

Fensterer v. *Pressure Lighting Co.,* 149 N. Y. Supp. 49.

Kavanaugh v. *Commonwealth Trust Co.,* 118 N. Y. Supp. 758, 767.

Pennsylvania Iron Works Co. v. *MacKenzie,* 190 Mass. 61.

If, by the simple expedient of appointing an Executive Committee to declare dividends, directors could avoid the statutory liability imposed by Sec. 23 of the Illinois Corporation Act of 1919, then that statute would be wholly nullified because directors could then appoint persons who were not directors on such committee and empower them to declare dividends. Clearly the Illinois legislature had no such intention when it enacted this statute.

Defendants argue that the word "assenting" as used in the statute cannot be construed to include approval and ratification of a dividend after it has been declared by the Executive Committee. However, inasmuch as the directors, when they created the Executive Committee and empowered them to declare dividends, could not relieve themselves of their responsibility for the declaration of dividends, then it is not necessary to consider the meaning of the word "assenting" because the directors "declared" the dividends when, pursuant to the authority which they gave, the Executive Committee declared the dividends. The simple doctrine of *respondeat superior* is applicable to this situation.

In the opinion of the Circuit Court of Appeals in the companion case of *DeMet's Incorporated* v. *Insull,* No. 822 on the Supreme Court's current docket of petitions for a

writ of certiorari, the Court aptly said (R. 346 in case No. 822):

> "In the instant case the Board of Directors empowered an Executive Committee to declare dividends, which of course did not operate to relieve them of the responsibility. We believe that a corporate director participates in a dividend, that is declares or assents to a dividend, under the statute, if he votes to give such an executive committee the power to declare a dividend and this is done, if he himself is an active member of the executive committee which declares a dividend, or if he approves, ratifies or assents to a declaration of the executive committee."

White-Wilson-Drew Co. v. *Lyon-Ratcliff Co.*, 268 Fed. 525, cited by defendants is wholly inapplicable since the allegations of the complaint in that case specifically negatived any participation by the directors in the affairs of the corporation and alleged that they had no knowledge of the wrongful acts, whereas in the case at bar the directors are affirmatively charged with active participation and with having declared or assented to the payment of dividends.

Both *Western Mortgage & Guaranty Co.* v. *Gray*, (Cal.) 8 Pac. (2d), 1016, and *Watkinson* v. *Adams* (Okla.) 103 Pac. (2d) 498, cited by defendants, are clearly distinguishable because the statutes there involved expressly excepted from liability those directors who were not present.

Section 23 of the Illinois Corporation Act of 1919 imposed liability on directors either for declaring or assenting to a dividend. "Assenting" obviously was intended by the legislature to mean something different from "declaring." This question had been directly presented to courts in other jurisdictions and they have uniformly held that ratification or approval of a dividend after it has been declared amounts to "assent":

Walker v. *Man*, 253 N. Y. S. 458, 466-467.

City Investing Co. v. *Gerken*, 202 N. Y. S. 41.

Cunningham v. *Shellman*, 164 Ky. 584, 598.
Williams v. *Brewster*, 117 Wis. 370, 383.
Calkins v. *Wire Hardware Co.*, 267 Mass. 52, 59.

C. *The complaint adequately alleges that the declaration of dividends was an impairment of capital and that dividends were declared while insolvent.*

Defendants cite no cases whatever in support of their contention that impairment of capital or insolvency is not adequately alleged and that the complaint contains mere conclusions. We have already pointed out that under the Rules allegations are sufficient if they contain a concise statement of the nature of the action charged and that details or evidentiary matter are not necessary.

The Circuit Court of Appeals properly held that it was sufficient under Illinois law to make general allegations of insolvency or impairment of capital at the time of the dividends, citing *Kelley* v. *Baggot*, 273 Ill. App. 580, 586, 587, wherein the Illinois court held that a general allegation of insolvency was sufficient, the actual total of assets and of liabilities being a matter of proof. To the same effect is *In re Claudon*, 73 Fed. (2d) 876 (C. C. A. 7).

In the original complaint, it is alleged that the dividends in question were declared and paid at a time when I. U. I. had no surplus. If I. U. I. had no surplus, the dividends could not have been paid except out of capital. It was not necessary for plaintiffs to allege details or plead evidence. The complaint alleges ultimate facts, not conclusions as defendants contend. The ultimate fact of declaring and paying dividends with no surplus out of which to pay them, is a sufficient allegation, either under former United States Equity Rule 25, or under Rules 8-a (2) and 8-e (1) of the present Rules of Civil Procedure, which have been fully discussed under sub-division A

above. These facts were peculiarly within defendants' knowledge.

Furthermore, the proferred amendments set forth in detail the capital structure of the company, its financial condition and its lack of any surplus at all times when the dividends in question were declared and paid (R. 330, 317).

D. *The complaint adequately alleges knowledge by defendants of the financial condition of I. U. I.*

Defendants contend that there are no allegations to show that defendants knew that the corporation was not in proper financial condition to pay the dividends and that they had a right to rely on the books. But according to the allegations of the complaint, these books showed that there was no surplus and on their face contained fictitious bookkeeping entries crediting certain transactions to surplus when in fact they did not represent earnings, in which transactions and booking entries the directors participated (R. 22-24).

Defendants' contentions are completely answered in the opinion of the Court of Appeals as follows:

> "In considering the question presently discussed, it is not, we believe, unreasonable to suppose that directors of a corporation ought to know whether the actual earnings authorize the withdrawal of the corporate assets to pay a dividend, since they alone are responsible for the declaration of dividends even though they may have delegated the power to a committee of their own." (R. 358).

The statute says nothing about knowledge of the company's condition, so that the liability is imposed irrespective of knowledge or lack of knowledge. Even apart from this, paragraph 48 of the original complaint alleges that each of the directors had, or in the reasonable exercise of his duties should have had knowledge, of all such matters

(R. 36) and the amendments likewise allege knowledge by defendants of the financial condition of the company as detailed in the amendments (R. 318).

Directors of a corporation are liable for the payment of improper dividend even though the corporate books show a surplus which was made up of fictitious income or profits. In *Moore* v. *Murchison*, 226 Fed. 679 (C. C. A. 4), a fictitious surplus was built up on the books of the company, out of which dividends were declared. The court said (p. 681):

> "It is difficult to speak of such a performance with moderation. The so-called surplus shown by these book entries was purely fictitious, and must have been known to be so by those in charge of the concern. * * * Directors cannot escape libility when they are in actual charge of the business of the corporation, and know, or ought to know, that the dividends they declare have not been earned."

Same in the following:

Cornell v. *Seddinger*, 237 Pa. 389.

Wesp v. *Muckle*, 120 N. Y. S. 976 (*affirmed* 201 N. Y. 527).

Union Discount Co. v. *MacRobert*, 234 N. Y. Supp. 529.

Quintal v. *Greenstein*, 256 N. Y. Supp. 462.

Chick v. *Fuller*, 114 Fed. 22 (1902), cited by defendants, exonerated only those directors who had not participated in the manipulation of the books and from whom the other directors had concealed indebtedness secretly incurred by them and which was not shown on the books. That is not comparable to the allegations in the case at bar.

E. *The record clearly shows that plaintiffs were creditors at the time the dividends were declared and paid.*

The Circuit Court of Appeals apparently was so little impressed with defendants' argument on this point that it did not even mention it in its opinion. As previously pointed out, paragraphs 13 and 16 of the original complaint (R. 11, 19) specifically allege that plaintiffs purchased their debentures about January 1, 1930, and that the same debentures which they then purchased remained unpaid and owned by the plaintiffs at the time of filing of this suit, namely, February 3, 1933. Therefore, it is clear that plaintiffs were creditors at all times during which dividends were paid after January 1, 1930, and prior to the bankruptcy in April 1932. It also alleges that other members of the public have owned other debentures since January 1, 1929 (R. 6).

In the face of the foregoing allegations defendants' contention that the complaint is fatally defective because it is nowhere alleged that plaintiffs were creditors when the dividends were declared and paid is simply absurd.

Furthermore, the cases cited by defendants are not applicable even if the above allegations did not appear. Both *Graham* v. *Railroad Company*, 102 U. S. 148, and *Chicago Daily News Co.* v. *Siegel*, 212 Ill. 617, merely held that creditors who had acquired their claims after alleged fraudulent acts occurred could not maintain suits to set aside those fraudulent transactions. In the instant case the rights of plaintiffs are not based on the law pertaining to fraudulent conveyances but under Section 23 of the Illinois Corporation Act giving creditors an additional remedy for the collection of their debts, without regard to when the dividends were declared. The case of *Buell* v. *Lanski*, 232 Ill. App. 500, cited by defendants, is not in point, the court there pointing out that the corporation had no creditors and was solvent when alleged wrongful

payments were made to officers by consent of the stock holders so that in no event was anyone injured.

On the other hand, in *Woolverton* v. *Taylor,* 132 Ill. 197, involving a suit under a statute similar to the one involved in this case, it appeared that plaintiffs acquired notes of a corporation by assignment, after the statutory liability was incurred, and the court held (page 212):

> "The officers, if liable at all, are liable to all the creditors of the corporation,—those existing prior to the contract creating the excessive indebtedness, those whose debts are created thereby, and also those who may afterwards become its creditors."

F. *This suit is brought in behalf of all creditors.*

We do not dispute defendants' contention that the liability under Section 23 of the Illinois Corporation Act of 1919 is personal to the creditors and that a suit to enforce the liability must be brought by one or more creditors on behalf of all creditors. The record shows that this suit was brought on behalf of all creditors (R. 2-3). The prayer of the bill is for judgment against the defendants in favor of the plaintiffs and all others similarly situated (R. 37). As a result of the so-called bank settlement referred to in *Aiken* v. *Insull,* case No. 821 before this court, the debenture holders of I. U. I. are its only creditors (R. 136-138).

G. *Section 23 of the Illinois Corporation Act of 1919 is not unconstitutional.*

Because the last sentence of the statute imposing the liability provides that a director shall be conclusively presumed to have assented to a dividend unless he was absent from the meeting, or unless his dissent therefrom is entered on the corporate records, defendants claim that this provision invades the judicial field and therefore the entire statute is unconstitutional.

The opinion of the Circuit Court of Appeals (R. 361) adequately disposes of this contention by pointing out that the statute imposing the liability is not dependent on the provision in question and that Section 23 with the last sentence omitted is not dissimilar in substance to its predecessor, Section 16 of the Corporation Act of 1872, the constitutionality of which has never been questioned. Furthermore, as pointed out by the Court of Appeals, defendants are not injured by the so-called conclusive presumption since plaintiffs have not thus far attempted to invoke that presumption. This Court should not be asked to review merely academic questions. The amendments charge defendants with actually voting for and assenting to the dividends. Certainly, if upon the trial the evidence should establish the defendants' liability without reference to that presumption, defendants will not have been injured at all.

The provision in question is not an essential and integral part of the statute as clearly appears from the fact that such statutory liability had been on the books of Illinois since at least 1872 without that sentence, so that it cannot be presumed that the legislature would not have enacted the statute without the provision in question, as was the case in *Chicago Motor Club* v. *Kinney*, 329 Ill. 120.

We believe the foregoing is a complete answer to defendants' contention; but even without that disposition of the point, the so-called conclusive presumption is not unconstitutional.

The statute does not provide that the absence of a director from a meeting must appear on the corporate records or that it is conclusively presumed that he is present when in fact he is absent. Hence, his absence may be shown by parol. A director may show that he was absent from the meeting and thus free himself from any conclusive presumption of assent. That does not suggest unconstitution-

ality. Likewise, his dissent, if entered in the corporate records, precludes any presumption against him. If the corporate records erroneously show him present, when in fact he was absent, or show assent instead of dissent, he still is not precluded from declaring the truth, for he may by an appropriate direct action have the records corrected in accordance with the facts:

Ford v. *Ford Mfg. Co.*, 222 Ill. App. 76, 82.
Dennis v. *Joslin*, 19 R. I. 666.
4 Fletcher's Ency. of Corps. (1933), p. 4051.
Venner v. *Chicago City Railway Co.*, 246 Ill. 170, 176.
Indian Refining Co. v. *Buhrman*, 220 Fed. 426.

Furthermore, the provision in question is not a conclusive presumption of evidence but is in reality a rule of substantive law, that is, it simply defines "assenting" to include the presence of a director at a meeting at which the dividend is declared and the failure of the director to dissent from the action. That effect would result if the words "conclusively presumed" were omitted from the clause. As has been shown, no director is prevented from having the records speak the truth or from proving his absence from a meeting and therefore he is not deprived of any right at the trial. The clause creates a rule of substantive law and not a rule of evidence (*In re Buchanan*, 171 N. Y. Sup. 708, 710; Wigmore on Evidence, 2d Ed. 1923, Section 1353).

Section 23 of the Corporation Statute and its predecessor, Section 16, have been enforced in a long line of decisions in this State. The fact that a statute has been sanctioned and acquiesced in for many years will have great weight with the Court in determining its constitutionality.

Cases cited by defendants are inapplicable. Neither *People* v. *Rose*, 207 Ill. 352, nor *Hall* v. *Woods*, 325 Ill. 114,

held the statutes there involved to be unconstitutional. *Carolene Products Co.* v. *McLaughlin*, 365 Ill. 62, condemned a statute because it declared something to be a fact which everyone knows is not a fact, that is, that the mixture of certain harmless, healthful food products produces an adulterous food and because any one accused of making such a mixture was denied any opportunity to rebut its presumed unwholesome character. That is not comparable to the situation here.

H. *The statutory liability is not penal but contractual.*

Defendants' contend that the statute is penal and therefore it cannot be enforced in equity, and further that the federal courts will not enforce a penal law of a state. But defendants err in their premise. Defendants are incorrect in arguing that the statute *prohibits* the directors from declaring such dividends and *punishes* them for violation of their duties. There is not one word in the statute, express or implied, which prohibits directors from declaring these dividends; the declaration of the dividends is not made illegal, it merely provides that directors will be answerable for the debts of the corporation in case they declare or assent to dividends under the circumstances stated. As stated by the Court of Appeals (R. 361):

> "It is, both in form and substance, a private obligation, similar, in many respects, to that of sureties, and it was intended to offer additional security to the creditors."

Citing:

Low v. *Buchanan*, 94 Ill. 76.
Woolverton v. *Taylor*, 132 Ill. 197.
Vestal v. *Robertson*, 277 Ill. 425, 431.
In re Beachy & Co., 170 Fed. 825, 828.

Defendants rely on *Vestal* v. *Robertson*, 277 Ill. 425, but that case is against their position and in favor of

plaintiffs. The court there, in considering a question under the statute of limitations, held one section of the Corporation Act to be a suit to recover a penalty where it made persons who assumed to exercise corporate powers *without complying with the provisions of the Act* personally liable for the debts contracted in the name of such pretended corporation. But the reason the court held that section to be penal was that the other provisions of the Act required, as a condition precedent to the exercise of corporate powers, that certain documents be filed with the Secretary of State and be recorded, the failure to do which gave rise to the penalty provision which was the basis of the suit. In other words, the Statute there *prohibited* the defendants from acting in a corporate capacity and *punished* them for having done so. That case particularly distinguished the case of *Woolverton* v. *Taylor,* 132 Ill. 197, in which it was held that subdivision 1 of the statute, which is involved in the case at bar, was not a penal statute because it contains no provision, express or implied, prohibiting directors from incurring liability in excess of the capital stock, but by imposing liability on directors therefor gave a contractual remedy directly to the creditors.

In re Beachy & Co., 170 Fed. 825, involving the statute at bar, pointed out that by a long line of decisions in Illinois it has been held that the Statute here involved is not penal but remedial and contractual in nature and is intended to furnish creditors protection in the nature of a suretyship; and that it is peculiarly a remedy to be enforced in a court of equity in a proceeding where the fund may be distributed among all creditors. Among the cases cited are *Hornor* v. *Henning,* 93 U. S. 228, *Low* v. *Buchanan,* 94 Ill. 76, *Woolverton* v. *Taylor,* 132 Ill. 197. Other cases to the same effect are *Pick* v. *Warshauer,* 244 Ill. App. 56; *Cairo Meal & Cake Co.* v. *Brigham,* 268 Ill. App. 510, *McCutcheon-Gerson Service* v. *T. & R. Co.,* 236

Ill. App. 261, *Seegmiller* v. *Day*, 249 Fed. 177, *Stone* v. *Chisolm*, 113 U. S. 302.

That the Federal Courts will enforce State statutes of this type abundantly appears from the foregoing cases, as well as *Huntington* v. *Attrill*, 146 U. S. 657 and *James-Dickinson Farm Mortgage Co.*, v. *Harry*, 273 U. S. 119.

I. *The proffered amendments were entitled to be filed.*

To supply the details which the District Court felt were lacking in the original complaint, plaintiffs offered certain amendments (R. 299-311, 317), which the District Court refused to allow, but which the Circuit Court of Appeals held should have been permitted. These amendments show in complete detail the part played by each defendant with respect to the authorization, declaration, approval or ratification of each dividend, the dates of the meetings, the names of the directors present at each meeting and how each voted, the amounts of dividends and details thereof, the capital structure of the corporation and its financial condition at the times when the dividends were declared.

The supplying of these details was not the statement of any new cause of action, nor did it change the plaintiffs' claim nor present a different theory of liability. They merely stated more fully the same matter contained in the original complaint. Therefore, the Statute of Limitations cannot affect the filing of the amendments. Under Rule 15-c of the Federal Rules of Civil Procedure, the amendments relate back to the date of the original pleadings. See *Echevarria* v. *Texas Co.*, 31 Fed. Supp. 596; *Perry* v. *Southern Railway Co.* 29 Fed. Supp. 1006, *White* v. *Holland Furnace Co.*, 31 Fed. Supp. 32, *Brown* v. *New York Life Insurance Co.*, 32 Fed. Supp. 443.

Even under the old rules the amendments would not be subject to the Statute of Limitations for the same reason

that they do not state a new cause of action but merely an amplification of the original pleadings. See *New York Central & H. Rd.* v. *Kinney,* 260 U. S. 340; *Clinchfield R. Co.* v. *Dunn* (C. C. A. 6, 1930) 40 Fed. (2) 586; *La Cueva Ranch Co.* v. *Brewer,* (C. C. A. 7, 1927), 23 F. (2) 369; *In re Claudon* (C. C. A. 7, 1934) 73 Fed. (2) 876, *Seaboard Airlines* v. *Renn,* 241 U. S. 290.

Under the Illinois law the rule is the same. (*Metropolitan Trust Co.* v. *Bowman Dairy Co.,* 369 Ill. 222).

Since the amendments are not barred by the Statute of Limitations, the Court of Appeals properly held that the mere lapse of time under the circumstances here did not justify the District Court in refusing to permit them to be filed and in dismissing the case.

It is clear that plaintiffs were not guilty of any unjustifiable delay. The record conclusively shows that under the District Court rules the defendants could have called up the motion to dismiss at any time (R. 330); that briefs of both sides as to the questions involved in the motions to dismiss had been filed by both sides and the matter taken under advisement by the District Court (R. 56); that by agreement of both sides disposition of the motions was continued generally (R. 59). The intervening period was devoted in the main to the disposition of the suits against the banks and their settlement (referred to in *Aiken* v. *Insull,* No. 821) which benefited defendants to the extent of the amount collected by debenture holders from the banks.

The ruling of the Circuit Court of Appeals that the amendment should have been permitted was in accordance with the spirit of the new Rules of Civil Procedure, Rule 15 (a), which provides that "leave shall be freely given when justice so requires." See *Mims* v. *Reid,* 275 Fed. 177 (C. C. A. 4); *McDonald* v. *State of Nebraska,* 101 Fed. 171 (C. C. A. 8); *Taylor* v. *Spurway,* 72 F. (2d) 97 (C. C. A. 5).

The decision of the Circuit Court of Appeals on these points is eminently just and in accordance with the applicable law of the State of Illinois and of the federal courts.

II.

The courts below correctly held that the complaint made a sufficient showing that the requisite jurisdictional amount is involved.

At the outset defendants are in the inconsistent position of asking this Court to affirm the District Court's judgment entered in their favor and, at the same time, of asking this Court to find that the District Court had no jurisdiction whatsoever.

In their cross-petition the defendants reargue the question of jurisdictional amount and present the same arguments on which they were overruled by the District Court and again by the Circuit Court of Appeals.

The first point argued by defendants (p. 24) is that "there is no basis for computing the amount of the dividend authorized or paid." The defendants admit that paragraph 43 alleges that a dividend of $1.39 a share on preferred stock was authorized but claim that there is no allegation as to how many shares of preferred stock were outstanding at that time. The defendants overlook paragraph 15 of the complaint in which it is definitely stated that the preferred stock issue amounted to 40,000 shares (R. 17).

The next point argued by defendants is that the complaint must affirmatively allege the facts to make it clear that the jurisdictional amount is present. The defendants persist in refusing to recognize the rule that so long as the complaint alleges in good faith that more than $3,000 is involved, it need not allege the evidence to prove the nature and extent of the damages. It is only when the

allegations in the complaint make it clear to a legal certainty that the claim is actually for less than the jurisdictional amount that the general allegation of jurisdictional amount will be disregarded. Defendants would reverse the rule by arguing that the complaint must affirmatively allege sufficient evidentiary facts to prove that the matter involves more than $3,000. The true rule has been recently repeated in *St. Paul Mercury Indemnity Co.* v. *Red Cab Co.*, 303 U. S. 293 (pp. 288-9):

> "The rule governing dismissal for want of jurisdiction in cases brought in the Federal Court is that, unless the law gives a different rule, the sum claimed by the plaintiff controls if the claim is apparently made in good faith. It must appear to a legal certainty that the claim is really for less than the jurisdictional amount to justify dismissal."

In their last argument the defendants object to the reference by the Circuit Court of Appeals to the plaintiffs' Counter Motions and Answers on Facts and the amendments to the complaint. Inasmuch as the Circuit Court of Appeals held that the plaintiffs are entitled to file their amendments to the complaint, the amended complaint may be considered as being the complaint now on file in this case in respect to which the defendants' attack is directed. There can be no question but that the amendments to the complaint, with their wealth of detailed information concerning the amounts and dates of the payments of dividends on the preferred stock, make it perfectly clear that many millions of dollars are involved in this suit and that the jurisdictional amount is present (R. 300-308). Of course, a complaint may be amended to cure whatever defects may exist in the original complaint as to the allegations of jurisdictional amount. In respect to the reference by the Circuit Court of Appeals to the plaintiffs' sworn Counter Motions and Answers on the Facts, the facts therein contained relating to jurisdictional amount

are in the Record (R. 251-3) and are admitted by the defendants (R. 282, 279-281, 289). These additional facts make it manifest that the jurisdictional amount is present.

In *Smith* v. *McCullough*, 270 U. S. 456, the court amended the complaint in order to have it include necessary jurisdictional facts appearing elsewhere in the record and said (p. 460):

> "The suit was begun in 1916; the parties had two hearings in each of the courts below; and the merits were exhaustively presented. In these circumstances to amend the bill now to conform to the jurisdictional fact indisputably shown elsewhere in the record will not subject either party to any prejudice or disadvantage, but will subserve the real interests of both. This court has power to allow amendments of this character (Rev. Stat. Sec. 954, Comp. Stat. Sec. 1591, 6 Fed. Stat. Anno. 2d ed. p. 98; *Norton* v. *Larney, supra; Realty Holding Co.* v. *Donaldson*, 268 U. S. 398, 69 L. ed. 1014, 45 Sup. Ct. Rep. 521), and the propriety of exercising it in this instance is obvious. We therefore shall treat the bill as amended, by our leave, to show the jurisdictional fact conformably to other parts of the record. With that fact brought into the bill, there can be no doubt that there was Federal jurisdiction."

In *Whalen* v. *Gordon*, 95 Fed. 305 (C. C. A. 8), the court said (p. 307):

> "The case appears to have been one, therefore, in which there was a sufficient amount in controversy to give the court jurisdiction, but the defendants in error had failed to plead it. Where the facts warrant the exercise of the jurisdiction of the court, but the pleader has failed to state them properly, the court is not deprived of the usual power to permit him to do so by amendment by the mere fact that the amendment will constitute or contain a jurisdictional averment."

The defendants conclude their argument on this point by stating that "on this ground of failure to allege facts as to amount involved to show jurisdiction in a federal

court the complaint was properly dismissed" (p. 25). It should be kept in mind that the complaint was not dismissed by the District Court for failure to properly allege the jurisdictional amount. The District Court concluded that it had jurisdiction of the parties and subject matter and except for the motions specifically allowed, all other motions, including the motion to dismiss for lack of the requisite jurisdictional amount, were denied (R. 297).

The cases cited by defendants are not in point. The first case cited by defendants, *Smith* v. *McCullough*, 270 U. S. 456, did not involve any question of jurisdictional amount and as pointed out above, it supports our position that the complaint may be amended by facts which appear elsewhere in the record. In another case cited by defendants, *Mutual Life Insurance Co.* v. *Thompson*, 27 F. (2d) 753, the court allowed an amendment to clarify the allegation as to jurisdictional amount and said (p. 755):

> "However, federal jurisdiction, in a case of this kind, is not necessarily defeated by even an impossibility of arriving at the exact value, or by difficulty in approximating the value, of the object sought by the bill. If this object has a pecuniary value, and if that value could exceed $3,000, the court cannot, on motion to dismiss, refuse to accept as true an allegation that the value of the object sought exceeds the jurisdictional minimum."

As to other cases cited by defendant, in *Hanford* v. *Davies*, 163 U. S. 273, no question of jurisdictional amount was involved, while *Norton* v. *Larney*, 266 U. S. 511, is another case in which the court itself amended an insufficient complaint to include jurisdictional facts appearing elsewhere in the record.

Hence, the positive allegation in the complaint that "the matter in dispute herein, exclusive of interest and costs, exceeds the sum of $3,000" (R. 3), must control as a sufficient allegation to base the jurisdiction of this Court and, in any event, the amendments to the complaint contain sufficient detailed evidence to satisfy anyone (R. 300-308).

III.

The decisions of the courts below, that the plaintiffs were not collusively selected in order to confer federal jurisdiction, are in accordance with applicable federal decisions.

At the outset, we should like to correct a typographical error in cross-petitioners' quotation from a portion of the opinion of the Circuit Court of Appeals (p. 25) wherein a portion of the opinion is quoted as follows:

> "The record presents a situation where certain creditors having a justifiable interest in the controversy * * *."

The word "justifiable" should properly read "justiciable" (R. 362).

The burden of cross-petitioners' argument with respect to collusive selection is that because out of 1500 debenture holders who were members of the debenture holders "Committee of 1,000" (one-third of whom being residents of Illinois) twenty-nine non-residents were chosen by the attorneys for the debenture holders or by a person acting at the behest of the attorneys, such manner of choosing plaintiffs amounted to collusion as would warrant the trial court in dismissing the cause for want of jurisdiction.

Cross-petitioners would have this Court believe that strangers to the litigation or "straw men" were plucked out of the air in order to create a spurious diversity of citizenship in order to gain access to the Federal Court. That is not true. The twenty-nine persons selected as plaintiffs were all owners of I. U. I. debentures, and had, prior to the institution of the suit, given their respective powers of attorney

> "to institute * * * any and all suits, actions and proceedings in the name of, or on behalf of, the undersigned * * * in any part of the world where such actions may be brought * * *." (R. 467.)

The most that can be said of cross-petitioners' position is that out of the large group of resident and non-resident debenture holders, a few non-residents were chosen to be plaintiffs in order to gain access to the Federal Court. That is definitely not collusion. The authorities are in complete accord that collusion with regard to maintaining suit in Federal Courts, as condemned in Section 37 of the Judicial Code (28 U. S. C. A. 80), is presented only by a situation where a person not a real party in interest and having no justiciable controversy is given or assigned a chose in action in order to create an artificial or spurious diversity of citizenship, or where a corporation which is the real party in interest designedly refuses to bring suit in order to enable a non-resident stockholder to maintain action in a Federal Court.

All but one of the cases cited by cross-petitioners involved situations where the party plaintiff was not a real party in interest, had no justiciable interest in the controversy and was a mere "straw man" or a stranger who was injected into the lawsuit merely to create a spurious diversity of citizenship. The other case cited by cross-petitioners, *Dawson* v. *Columbia Trust Co.*, 197 U. S. 178, was not strictly speaking a question of collusive selection but turned upon the proposition that a necessary party was made a party defendant to create a false diversity of citizenship when that person obviously should have been joined as a party plaintiff.

It has been enunciated by this Court in numerous decisions that so long as a basis for Federal jurisdiction actually exists, the courts will not inquire into the motive behind the preference for a Federal rather than a State forum. That proposition was decided by this Court in the *Matter of Reisenberg*, 208 U. S. 90, wherein this Court said (p. 111):

> "So long as no improper act was done by which the jurisdiction of the Federal court attached, the motive for bringing the suit there is unimportant."

In

Black and White T. & T. Co. v. *Brown and Yellow T. & T. Co.*, 276 U. S. 518,

this Court held that the action of a Kentucky corporation doing all its business in that state in dissolving and reforming under the laws of Tennessee for the sole purpose of enabling it to gain access to the Federal courts in a contemplated action against another Kentucky corporation, was not collusive, and said (524):

> "The motives which induced the creation of respondent to become successor to its Kentucky grantor and take a transfer of its property have no influence on the validity of the transactions which are the subject of the suit. The succession and transfer were actual, not feigned or merely colorable. In these circumstances, courts will not inquire into motives when deciding concerning their jurisdiction."

A case identical to the one at bar as respects the question of collusive selection, is that of

New Albany Waterworks v. *Louisville Banking Co.*, 122 Fed. 776 (C. C. A. 7).

There a bill was filed in the Circuit Court of the United States for the District of Indiana by a Kentucky corporation, plaintiff, as a stockholder of an Indiana corporation, defendant, to set aside a lease and for injunctional and other relief. In addition to the Indiana corporation, five of its directors and the City of New Albany, Indiana, were also made defendants. Objection to the jurisdiction of the court was made on the ground that while the suit was motivated by a group of stockholders, many of whom were residents of Indiana, said group chose a nonresident stockholder to become the plaintiff in order to confer federal jurisdiction. Appeal there was had from an order in the trial court granting an injunction and appointing a receiver. The order was affirmed and the court said as respects the question of jurisdiction, at 778-9:

> "The appellants' objection to jurisdiction of the bill

> is untenable. It rests upon the proposition that the answer charges, without denial, that certain of the minority stockholders of the defendant New Albany Waterworks, who are citizens of Indiana, 'combined with the appellee, a citizen of Kentucky, and caused it to bring the suit' in the federal court. * * * Neither the fact of citizenship of the other stockholders, majority or minority, nor of their attitude to the controversy, by contribution or otherwise, is material to relief under the bill, if the management of the corporation is adverse to the objects of the bill, and is not in collusion with the complainant in any sense."

That decision clearly enunciates the proposition that it is not collusive or in any way wrongful for a class of stockholders or creditors, as the case may be, to choose one or more persons of the class to become the named plaintiffs in order to confer federal jurisdiction, as long as such plaintiffs have a real and justiciable interest in the controversy. Furthermore, it is difficult to see how it can be said that plaintiffs had no "justiciable interest" when it is not disputed but that they are actual bona fide owners of the debentures sued on. In other words, it is not denied that they had an actual interest subject to being litigated.

Another case wherein selection of plaintiffs was had in a manner similar to the one at bar was that of

> *Hutchinson Box Board and Paper Co.* v. *Van Horn*, 299 Fed. 424 (C. C. A. 8),

an action by a non-resident stockholder against the corporation in which he owned stock and another corporation to cancel a contract between the two. The action was brought in the United States District Court for the District of Kansas. It appeared that the named plaintiff, who was a resident of Colorado, had contacted a Kansas attorney named Malloy with reference to a proposed suit and that Malloy desired to bring suit in the Federal Court.

Subsequently, Malloy learned that certain local stockholders contemplated bringing an identical suit in the state court but preferred, however, that it might be brought in the Federal Court; whereupon negotiations were had between the plaintiff and the local stockholders which resulted in a contract between all such stockholders to the effect that the non-resident would bring suit in his name in the Federal Court; that he would not dismiss the same without the consent of the local stockholders and that the latter would indemnify him for any expenses, etc. Motion to dismiss for lack of Federal jurisdiction was made on the ground of collusion between the plaintiff and the local resident stockholders, which alleged collusion was predicated upon the contract between the two groups. This motion was overruled and upon trial decree was had for plaintiff. On appeal, the decree was affirmed. With respect to the question of collusion, the court said (429):

> "And as said by the court in the *Albany Waterworks* case, *supra*, the fact that local stockholders may have induced him to file the bill and contributed to the expense does not make the suit collusive. * * * The utmost that can be said of the contract is that appellee therein agreed, in consideration of a contribution, on the part of certain local stockholders, to the preliminary expenses, to commence and prosecute the action in good faith for the benefit of all interested parties, and not to make a compromise of the litigation beneficial to himself and detrimental to the general interests. This in our opinion is not sufficient to make the contract collusive."

The court in the above cited case went much farther in holding there was no collusion than is necessary in the case at bar. In that case there was a contract between local stockholders and a non-resident stockholder that the latter should maintain suit in his name and that he would be indemnified and his expenses paid by the local stockholders. In the case at bar the most that could be said to

support the claim of collusion is that out of the group of creditors certain non-residents were chosen to bring suit, and there is no element of a contract for indemnification, etc., as existed in the *Hutchinson* case.

Cross-petitioners appear to rely principally upon *Dawson* v. *Columbia Trust Co.*, 197 U. S. 178, to the effect that:

> "When the arrangement of the parties is merely a contrivance between friends for the purpose of founding a jurisdiction which otherwise would not exist, the device cannot be allowed to succeed." (Cross-Petition, p. 28.)

However, as we have heretofore stated, the *Dawson* case was not one of collusive selection but merely of improper alignment of parties for the purpose of creating a spurious diversity. In the instant case there has never been even a suggestion that the parties in the litigation have been aligned in other than their true or normal position in the controversy.

Even without the full and extensive authority contained in the uniform contract involved here, it is perfectly permissible for attorneys representing a large class or group of creditors or stockholders to pick at random a few from the group to become named plaintiffs, or to choose several non-residents from the group in order to confer federal jurisdiction, *as long as the named plaintiffs chosen are bona fide members of the class, have a justiciable interest in the controversy and are not mere "straw men" brought into the picture from outside the class.* The fact that the secretary of the committee, acting under the direction of the attorneys, may have performed the actual "picking" rather than the attorneys personally, is not worthy of discussion.

IV.

Plaintiffs' attorneys had authority to commence and prosecute this suit.

Defendants filed a motion to require plaintiffs' attorneys to show by what authority they had commenced and were prosecuting this suit (R. 471). Plaintiffs' attorneys replied setting forth written contracts from each of the several plaintiffs (R. 474). These contracts employed plaintiffs' attorneys

> "1. To collect all moneys due upon the Insull Utility Investments, Inc., Debentures listed below the name of the undersigned.
>
> "2. To institute, prosecute, join and participate in any and all suits, actions and proceedings in the name of, or on behalf of, the undersigned and that you may deem advisable in furtherance of such collection, in any part of the world where such actions may be brought or may at any time be pending." (R. 467.)

There was a hearing in the District Court on the question of whether this document was sufficient authority to authorize plaintiffs' attorneys to file this suit in the light of all the circumstances (R. 488). Among the circumstances surrounding the execution of this document was the fact that the Insull Debenture Holders Protective Committee had sent out a letter to debenture-holders on October 5, 1932, urging that each addressee join with the committee and execute the contract quoted from above, a copy of which was enclosed with each letter. These letters stated, among other things, that the Committee's attorneys were "laying the foundation for suits to establish liability against directors who voted * * * dividends from capital" (R. 478). A similar letter sent out October 20, 1932, stated that the Committee's attorneys had elicited information tending to establish "liability of directors who voted * * * dividends from capital" (R. 479).

The statement in the last sentence of part IV of the cross-petition that the contracts were "solicited in connection with the bankruptcy proceeding" is not supported by the record and is not true.

We have no quarrel with the principle of law urged by defendants in part IV of their cross-petition. A suit commenced by an attorney without color of authority from the plaintiff is admittedly a nullity. In this case there was specific written authority to collect moneys due upon the debentures and to institute any suit deemed advisable in furtherance of such collection. Nothing in the contract purported to limit the sources of that collection to the funds of Insull Utility Investments, Inc., the obligor on the debentures. On the contrary every circumstance surrounding the execution of these contracts and, indeed, the contracts themselves, show beyond any doubt that the parties to the contract (the debenture-holders and plaintiffs' attorneys) contemplated collection from other sources.

In the first place, Insull Utility Investments, Inc., had been adjudicated a bankrupt. The fact that the assets in the hands of the receiver in bankruptcy had a value of but a minute fraction of the total of its obligations had been widely publicized. Enclosed with the above-quoted letters of October 5 and October 20, 1932, there was, in addition to the contract, a form for filing proof of claim in bankruptcy, which included a power of attorney running to the senior partner of each firm of attorneys representing plaintiffs (R. 483). No action beyond the filing of proof of claim in bankruptcy was necessary, or indeed could have been undertaken, to collect from the assets of the bankrupt whatever small percentage of his claim each debenture-holder might expect to receive from that source. The contract was obviously for the purpose of employing attorneys to collect the money due the debenture-holder

from other sources. Any other construction makes paragraph 2 of the contract quoted above completely meaningless. Further, in that part of the contract dealing with compensation of plaintiffs' attorneys there was a specific reference to "any proceeding at law, equity or bankruptcy" (R. 468).

Defendants argue that this is not a suit to collect moneys due upon the debentures but is a penal action against persons who are not parties to the debentures. As shown in part I-H of this brief, this suit is not penal in character. On the contrary, it was held by the Supreme Court of Illinois in *Woolverton, et al.* v. *Taylor, et al.*, 132 Ill. 197, that when, by reason of some provision of the Illinois Business Corporation Act, directors become personally liable for the debts of the corporation, that liability is not penal but in the nature of security to the creditors. An attorney employed by a client to collect all moneys due on an obligation not only has the authority to look to the security for that obligation, but would be negligent in his duty and subject to censure if he failed to make every effort to resort to such security to collect the money due to his client.

The liability of the directors to plaintiffs is clearly based upon the debentures and the ownership thereof by plaintiffs. If no money were due them upon the debentures, this suit could never have been started. The principal amount of the debentures plus accrued interest clearly limits the liability of the directors. A suit against the directors was exactly what was contemplated by the contract. Defendants' contention requires that all of the surrounding circumstances be ignored, that all of the contract itself be ignored except paragraph 1 quoted above, and that to paragraph 1 there be attributed a meaning strained and twisted out of all recognition.

In defendants' cross-petition there is an indication that

only five of the plaintiffs were advised of the filing of this suit. Since all plaintiffs had given written authority to start the suit, notice of its filing is immaterial with respect to the question of plaintiffs' attorneys' authority and, in fact, every plaintiff was notified (R. 474).

Since the District Court ordered, adjudged and decreed that the attorneys for plaintiffs had established their authority to commence this suit, and since no appeal from that order was taken by defendants, the question is not reviewable by this court.

The District Court ordered, adjudged and decreed that the attorneys for plaintiffs had established their authority to commence this suit (R. 321). The defendants did not file any appeal or cross-appeal from this portion of the decree. Plaintiffs therefore objected to the consideration of this matter in the Circuit Court of Appeals. Nevertheless, the matter was considered by the Circuit Court of Appeals which, in its opinion, stated:

> "The District Court investigated this matter thoroughly and concluded that the attorneys for plaintiffs had authority to prosecute these proceedings. We see no reason for disturbing this conclusion." (R. 362.)

The law is well-settled that an appellee who has not filed a cross-appeal can properly address his argument only to matters in support of the decree below, and is precluded, by failing to cross-appeal, from urging any matter in derogation of the trial court's decree or any portion thereof. In *Peoria & P. U. R. Co.* v. *U. S.*, 263 U. S. 528, suit was instituted by a railroad to enjoin the enforcement of an Interstate Commerce Commission order. The Government objected to the venue and was overruled. The injunction sought was denied and the suit dismissed. On appeal to the Supreme Court the Government, in addition to arguing the merits, also contended that the decree

should be affirmed because its objection to the venue should have been sustained. This Court, however, held that by failing to interpose a cross-appeal, the Government was precluded from again raising the question of venue. We see no reason why this Court should adopt a different rule in the case at bar.

Even if the relief which might have been sought by cross-appeal would have been substantially the same as that already received by the defendants, still, if it differs in any degree from that awarded in the decree appealed from, then it is up to the defendants as appellees to have saved their question by cross-appeal. See *Morley Construction Co.* v. *Maryland Casualty Co.*, 300 U. S. 185, 191.

V.

Both the District Court and the Court of Appeals properly held, in accordance with the Illinois law, that the covenants not to sue given four of the defendant-directors did not discharge the other defendant-directors.

In June, 1937, the defendants and their counsel discussed with representatives of the plaintiffs the advisability of joining with the banks in the settlement of the claims of the debenture holders against them or in purchasing their peace by obtaining covenants not to sue (R. 242). The attorneys for defendants, Ferguson and Tobey, presented to plaintiffs' attorneys information concerning the financial responsibility of their clients and facts to show that a large decree against them could not be collected. For the purpose of avoiding further defense of the suit as to them, but so as not to prejudice this suit as to the other defendants, those two defendants proposed to pay sums within their means in consideration of covenants not to sue them further (R. 243).

Thereupon, in accordance with the provisions of their contract of employment, plaintiffs' counsel presented the

matter to the executive committee of the Insull Debenture Holders Protective Committee of 1,000, and pursuant to due resolutions adopted by that committee, Lewis F. Jacobson, under date of July 17, 1937, executed to the defendants, Tobey and Ferguson, covenants not to sue in consideration of $7500.00 paid by each of them (R. 244).

The covenants not to sue (R. 269) are in the usual form of such instruments and specifically provide that neither the transaction nor the instrument is or intended to be a release or discharge of any one, including the covenantees, nor an accord or satisfaction, nor a settlement discharging any claim or cause of action, nor that the money paid thereunder was accepted or received as compensation (R. 269-271). In addition, the covenantees acknowledged that the instruments expressed the complete transaction and intention of the parties (R. 272).

Pursuant to the above, on July 17, 1937, an order was entered by the District Court on stipulation dismissing this suit as to the defendants, Tobey and Ferguson (R. 64).

Some months later similar arrangements were made with the defendants Budd, who paid $10,000, and Brewster, who paid $25,000. Similar covenants were given them (R. 244-245) and on October 4, 1937, on stipulation they were dismissed as defendants in this suit (R. 65).

The amount of the damages to the plaintiffs and the other debenture holders is greatly in excess of the $50,000 paid by these four defendants (R. 246). In fact, the statutory liability of defendants for declaring dividends out of capital is over $7,000,000 (R. 252).

The District Court denied defendants' Second Motion for Summary Judgment and held that "the effect of the settlement with the four defendants was a covenant not to sue and therefore not a bar to this action" (R. 298). The Circuit Court of Appeals found that the conclusion of the District Court on this point was correct (R. 363).

In Illinois it is clearly settled that a covenant not to sue given to one or more joint tort-feasors is not a bar to prosecution of the cause to action against the other joint tort-feasors. These principles are clearly stated in the leading case on the subject, *City of Chicago* v. *Babcock*, 143 Ill. 358, in which the Court said (p. 366):

> "Where there are a number of tort-feasors, the party injured may, at his election, sue one, or several, or all; and where the suit is against one or some of the wrongdoers, but not against all, the person or persons sued have no right to complain. And so, also, where there is suit against several tort-feasors, the dismissal of the suit against one does not bar the action against the others. (*Knapp* v. *Roche*, 94 N. Y. 329; *Sloan* v. *Herrick*, 49 Vt. 327; *Bloss* v. *Plymale*, 8 W. Va. 393).
>
> "A *release* to one of several joint tort-feasors is a release to all, and an accord and satisfaction with one of them is a bar to an action against the others.
>
> "Here, there is no claim of a technical release under seal. The pending suit against LeCardi was dismissed, and a written agreement was signed that no action should be begun against LeCardi by appellee. This, on its face, was simply an agreement or *covenant not to sue*. The legal effect of such a covenant is not the same as that of a release.
>
> "A covenant not to sue a sole tort-feasor is, to avoid circuity of action, considered in law a discharge, and a bar to an action against such tort-feasor. But the rule is otherwise where there are two or more tort-feasors, and the covenant is with one of them not to sue him. In such case the covenant does not operate as a release of either the covenantee or the other tort-feasors, but the former must resort to his suit for breach of the covenant, and the latter cannot invoke the covenant as a bar to the action against them."

Defendants do not challenge this well-established rule but argue that notwithstanding the fact that the instrument was in the form of a covenant not to sue, the circumstances show that there was in fact a release or accord and satisfaction. Their contention is not supported by any evidence

whatever but simply on two arguments (defendants' brief, p. 33). The first is that it is incredible that four of the defendants would have paid $50,000 merely for a contract that they would not be sued, that they must have been convinced that they would be free from any further liability, and that a suit brought at this late date would be barred by laches and the Statute of Limitations.

This argument of the defendants is without any substance whatsoever. Defendants do not make a single reference to the Record to support their argument. There is absolutely nothing in the Record to suggest even remotely that the parties intended to execute a release or an accord and satisfaction. Nothing in the Record contradicts the actual terms of the covenant not to sue or the acknowledgment by the covenantees that the covenant accurately states the nature of the transaction (R. 269-272).

It clearly appears that the liability of the defendants runs into millions and that the $50,000 did not pay those damages in full nor was it accepted as full compensation of those damages. It therefore is manifest that defendants cannot rely on the exception laid down in the *City of Chicago* v. *Babcock, supra,* relating to an actual accord and satisfaction.

The argument that the four directors would not have been foolish enough to pay $50,000 simply for covenants not to sue is absurd. They were faced with possible judgments against them for millions of dollars and expensive litigation. They had the advice of experienced counsel and were satisfied that it was desirable to purchase their peace for relatively nominal sums. In any event, they bargained for covenants not to sue, paid their money for covenants not to sue, and the Illinois law in respect of covenants not to sue controls the situation.

The defendants' argument that they are released because four of the defendants were dismissed from the case

and a suit brought at this late date against the four defendants would be barred by laches and the Statute of Limitations, is contrary to the Illinois law. That is established not only by *City* v. *Babcock, supra,* but also by many other cases in Illinois following the same principles, such as:

Chicago & Alton Ry. Co. v. *Averill,* 224 Ill. 516, 517, 521.
West Chicago St. R. R. Co. v. *Piper,* 165 Ill. 325, 338.
Puck v. *City of Chicago,* 281 Ill. App. 6, 11.
Onyschuk v. *Vincent,* 277 Ill. App. 414, 428.
Baxter v. *Rothschild,* 204 Ill. App. 346 (Abst.).
Balsley v. *Hetzel,* 182 Ill. App. 136 (Abst.).
Gore v. *Henrotin,* 165 Ill. App. 222, 225, 226.
Vandalia R. R. v. *Nordhaus,* 161 Ill. App. 110, 113.
City of Chicago v. *Smith,* 95 Ill. App. 335, 336, 339.

In certain cases, such as *Purinton* v. *Belt Railroad,* 204 Ill. App. 382, *Gore* v. *Henrotin,* 165 Ill. 222, *Scharfenstein* v. *Forest City Knitting Co.,* 253 Ill. App. 190, the action was brought under the State Wrongful Death Act, which requires such actions to be brought within one year. Notwithstanding that fact certain defendants in those cases were dismissed and covenants not to sue given them, and in the reviewing courts several years later, it was held that the other defendants were not discharged.

The second argument raised by defendants, that Mr. Jacobson had only authority to execute releases and had no authority to execute covenants not to sue, and therefore the covenants not to sue must be treated as releases, is absurd on its face. He had general authority "to execute and acknowledge any document or instrument whatsoever in furtherance of the collection of money due on said debentures" (R. 467-468). This language is certainly broad enough to include a covenant not to sue. Fur-

thermore, the power of attorney provided that a settlement of less than par required approval of the Executive Committee and the Executive Committee approved the matter and directed Mr. Jacobson to execute covenants not to sue (R. 244, 268, 270).

Even if there were any merit of defendants' contention that the authority contained in the powers of attorney was exceeded or improperly exercised, the only ones who could complain would be the debenture holders in whose behalf they were given. It could not possibly accord the defendants any right to claim that the instruments were not covenants not to sue and that they had been released.

The question here involved has been amply presented, considered and properly determined by both the District Court and the Circuit Court of Appeals.

Conclusion.

The defendants' cross-petition fails to furnish any reason for the review by this Court of that portion of the judgment of the Circuit Court of Appeals which is in favor of the plaintiffs. The portion of the judgment under attack is not final and this Court should not burden itself with the review of preliminary matters which may become moot before the case is ended. Moreover, the judgment is not in conflict with applicable decisions of the state and federal courts.

For all these reasons, respondents urge that the cross-petition for certiorari be denied.

Respectfully submitted,

EDMUND D. ADCOCK,
ROGER Q. WHITE,
LEWIS F. JACOBSON,
Counsel for Cross-Respondents (Plaintiffs).